In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 212

A. GUSMER, INC., A CORPORATION, PETITIONER

v.

JAMES P. McGRANERY, ATTORNEY GENERAL OF THE UNITED STATES, AS SUCCESSOR TO THE ALIEN PROPERTY CUSTODIAN

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 55) is not reported. The opinion of the Court of Appeals (R. 59) is reported at 196 F. 2d 860. The opinions of the Hearing Examiner, Office of Alien Property (R. 37) and the Director of that Office (R. 48) are not reported.

JURISDICTION

The judgment of the Court of Appeals was entered April 24, 1952 (R. 65). The petition for a writ of certiorari was filed July 21, 1952. Jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether, in a proceeding to enforce a debt claim under Section 34 of the Trading with the Enemy Act, a corporation, which for eight years remitted income to an alien without withholding the tax thereon as required by the Internal Revenue Code and which, after the vesting of the alien's property, was compelled to pay such taxes, is entitled to be subrogated to the tax claim of the Collector against the alien's vested property?

STATUTES INVOLVED

The pertinent provisions of the Trading with the Enemy Act and of the Internal Revenue Code are set forth in the petition at pp. 3-8.

STATEMENT

The facts are not in dispute. In 1933, petitioner entered into an agreement with a German corporation, Chemische Werke Marienfelde, for the right to use a secret process and trademark. In exchange, petitioner paid a lump sum of $3,000 to the alien corporation and also agreed to pay annual license fees based on sales (R. 20-30). From 1933 to 1941, it remitted to the alien the entire amount of the fees coming due under the agreement without filing a return for income taxes on the remittances or with-

holding and paying such taxes, as required by Section 143 of the Internal Revenue Code (53 Stat. 60, as amended, 26 U.S.C. § 143) (R. 10, 34).

In 1941, petitioner discontinued further remittances as a consequence of the federal "freezing" program which prohibited, except as licensed, transactions involving property in which nationals of designated foreign countries, including Germany, had an interest (Executive Order No. 8389, April 10, 1940, 5 F.R. 1400, as amended by Executive Order No. 8785, June 14, 1941, 6 F.R. 2897). The unremitted fees then accrued to the credit of the alien on petitioner's books. In May 1946, the Alien Property Custodian[1] vested, among other things, the right of the alien to the fees which had accrued since 1941 (R. 5-7). Petitioner accordingly paid the accrued fees to the Custodian. As to these fees, petitioner did withhold a portion for income tax purposes and in July 1946 paid the amount withheld to the Bureau of Internal Revenue (R. 55).

As to the fees which petitioner had remitted to the alien during the 1933-1941 period without, however, withholding and paying the income taxes, the Commissioner of Internal Revenue in 1947 determined that a deficiency of $13,363.88 was due. Petitioner paid this sum on October 20, 1947 and on February 10, 1948 paid an additional $3,340.98 in

[1] The functions of the Alien Property Custodian were transferred to the Attorney General by Executive Order No. 9788, October 14, 1946, 11 F.R. 11981. The term "Custodian" will be used interchangeably to refer to the former Alien Property Custodian or to the Attorney General as his successor.

penalties and $6,056.53 in interest, making a total of $22,761.39 (R. 10, 34).

Thereafter in 1948 petitioner filed with the Custodian its claim under Section 34 of the Trading with the Enemy Act (40 Stat. 411, as amended, 50 U.S.C. App. § 34) for the $22,761.39 plus interest against the vested assets of the alien. (R. 9, 33) [2] After oral argument and submission of briefs, the Hearing Examiner dismissed the claim (R. 37). On appeal, the Custodian affirmed (R. 48). Petitioner then filed its complaint in the District Court pursuant to Section 34(e) of the Act to review the Custodian's determination (R. 2).[3] The District Court dismissed the complaint on the merits, thus upholding the Custodian's determination (R. 55).[4]

The Court of Appeals also affirmed (R. 59), holding: (1) that any claim which petitioner may have against the alien arose after vesting when petitioner paid the taxes; hence, its claim to reimbursement out of the alien's vested assets is barred by Section 34(a) because "not due and owing at the time of * * * vesting"; and (2) that in all circumstances "the dominant equities preclude a right of subrogation [to the Collector of Internal Revenue] * * *

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[2] In the court below, petitioner abandoned its claim for the $3,340.98 in penalties (R. 64).

[3] The action was brought against J. Howard McGrath, as Attorney General and successor to the Alien Property Custodian. James P. McGranery was duly substituted as defendant.

[4] Initially, cross-motions for summary judgment were denied by the District Court, because it was thought there was an issue of fact. See *A. Gusman* [sic] v. *McGrath*, 94 F. Supp. 724. When the case came on for trial, however, neither party introduced any evidence or disputed any fact (R. 60, note 1).

as a substitute for [petitioner's] failure to perform a statutory duty which if performed would have obviated its present claim." (R. 63) Accordingly, the Court felt it unnecessary to reach the question whether the scheme adopted by Congress for the disposition of vested property precludes subrogation, quite apart from the equities (R. 63).

ARGUMENT

The question presented is limited in scope and is of little consequence generally. As the Court of Appeals noted (R. 62, note 3),[5] the case does not involve the general question whether a withholding agent, compelled to pay income taxes not withheld, has a valid claim for the amount so paid against the alien to whom the income was remitted in full. Nor does the case concern whether the agent in such circumstances may reach the unvested assets of the alien. Furthermore, the decision below does not reach the question whether, in a proceeding to enforce a claim against vested assets, the remedy of subrogation is precluded by the scheme adopted by Congress for the disposition of vested property. The only question decided below is whether the equities of this particular case will support the remedy of subrogation against vested assets in favor of petitioner.

The decision below denying the benefits of subrogation to petitioner because delinquent and because allowance would prejudice the interests of

[5] "We are not now confronted with any question as to the alien's independent obligation to [petitioner] or as to assets not vested."

innocent third persons conforms to principles governing subrogation announced by this Court and other courts. It also accords with *Synthetic Patents Co.* v. *Sutherland,* 22 F. 2d 491 (C.A. 2), certiorari denied, 276 U.S. 630, decided on virtually identical facts and on comparable provisions of the Act in effect in World War I.

There is no conflict of decision. *McGrath* v. *Dravo Corporation,* 183 F. 2d 709 (C.A. 3), asserted by petitioner to be in conflict (Pet. 9, 15), contains not a single reference to subrogation and on its facts could not possibly involve the doctrine. Manifestly, there is no important question of federal law requiring decision by this Court.

1. During the years 1933 to 1941, petitioner failed to withhold and pay the tax due on income which it remitted to a non-resident alien corporation.[6] Having been compelled in 1947 to pay that tax,[7] it now seeks under Section 34 of the Trading with the Enemy Act to be made whole out of the alien's vested assets, which have already borne the full share of income taxes incident to them.

(a) Assuming a claim for reimbursement arose in favor of petitioner when it paid the 1933-1941 taxes, such claim did not come into being until after

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[6] A person having control over the income of a non-resident alien, as did petitioner, is required to deduct and withhold the amount due as income tax. Section 143(b) Internal Revenue Code, 53 Stat. 60, as amended, 26 U.S.C. § 143(b). By Section 143(c), such person is required to make a return thereof, to pay the tax and, in addition, is expressly "made liable for such tax."

Section 144 in effect makes Section 143 applicable to the income of foreign corporations.

[7] Plus penalties and interest.

the vesting of the alien's property. The property was vested in May, 1946 and petitioner did not pay the taxes in question until October, 1947. Accordingly, such claim as it did acquire is barred by the explicit terms of Section 34(a), which declares:

> No debt claim shall be allowed under this section if it was not due and owing at the time of such vesting * * *.

In *Synthetic Patents Co.* v. *Sutherland,* 22 F. 2d 491 (C.A. 2), certiorari denied, 276 U.S. 630, decided under comparable provisions of the Act in effect in World War I, the claimant, like petitioner in the instant case, was compelled to pay non-withheld taxes in 1919, after the cut-off date of Section 9(e) which required that a debt claim against vested assets be "owing to and owned by the claimant prior to October 6, 1917." The court held, as an alternative ground for denying relief,[8] that the claim, assuming one, did not arise prior to October 6, 1917 and was therefore not allowable (22 F. 2d at 494).[9]

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[8] The other ground was that the claimant, as withholding agent, is individually liable for non-withheld taxes and that the agent's subsequent payment does not give rise to a claim against the alien's funds in the hands of the Custodian (22 F. 2d at 493).

[9] Petitioner's distinction of the *Synthetic Patents* case, *supra,* on the basis of the difference in the restrictive language of Section 9(e) and 34(a) does not advance its position (Pet. 19). The time limitation in Section 34(a) quite clearly represents the World War II counterpart of Section 9(e) and resulted in part from the holding of this Court in *Markham* v. *Cabell* (326 U.S. 404) that the restriction of Section 9(e) was applicable only to World War I debt claims. See S. Rept. No. 1839, 79th Cong., 2d Sess., pp. 3-4; H. Rept. No. 2398, 79th Cong., 2d Sess., p. 9.

(b) To avoid the effect of the time limitation in Section 34(a), petitioner seeks to avail itself of the remedy of subrogation. It argues that as each payment was made to the alien in the years 1933 to 1941, the alien owed taxes to the Collector on the amount received and that these taxes were debts "due and owing," within the meaning of Section 34(a), prior to vesting. Petitioner then asserts that by virtue of its payment of these debts it should be subrogated to the tax claims of the Collector against the alien (Pet. 14-19).

Petitioner's reliance on this remedy is misplaced. Subrogation is, of course, an equitable remedy granted or withheld as the circumstances of each case warrant. *Gray* v. *Jacobsen,* 13 F. 2d 959 (C.A.D.C.). It will not be applied to relieve a claimant from the results of his own delinquency. *German Bank* v. *United States,* 148 U.S. 573, 580-581. Nor can it be availed of by one not alert in discharging his duty or guilty of inequitable conduct. *American Surety Co.* v. *Bethlehem Bank,* 314 U.S. 314, 317. Cf. *United States* v. *Ryder,* 110 U.S. 729, 737. Under the circumstances of this case, petitioner is scarcely in a position to seek the benefits of that remedy, for performance of its statutory duty to withhold taxes would have obviated its present claim, and its own neglect extending for a period of eight years created the problem.

Also militating against application of subrogation is the effect its allowance would have on the interests of innocent third persons. See *Washington Mechanics' Sav. Bank* v. *District Title Ins. Co.,*

65 F. 2d 827 (C.A.D.C.); *Gray* v. *Jacobsen*, 13 F. 2d 959 (C.A.D.C.). By the War Claims Act of 1948 (62 Stat. 1240, as amended, 50 U.S.C. App., Supp. IV, §§ 2001 *et seq.*), Congress has provided that the net proceeds of vested assets shall be used to compensate American war claimants, principally internees and prisoners of war mistreated by the enemy. Allowance of petitioner's claim would diminish *pro tanto* the fund available for these purposes. The effect of such allowance would be that the vested license fees for 1941-1948, out of which income taxes for those years have already been paid, would be required to bear in addition the taxes attributable to the 1933-1941 license fees, which petitioner improperly failed to deduct from its payments to the alien during those years. Thus as between the war claimants and petitioner, the equities clearly favor the former, since petitioner's loss for which it seeks to be made whole, was occasioned by its own delinquency. Accordingly, the court below was manifestly correct in holding that "in all these circumstances the dominant equities preclude a right of subrogation * * *." (R. 63).

(c) As an argument against denying the benefits of subrogation, petitioner offers only a hypothetical explanation for its failure to withhold. While conceding that "in the present case, there is no evidence as to why petitioner failed to withhold and pay the taxes * * *" (Pet. 21), it suggests the theoretical possibility that its omission could have been caused by a misunderstanding of the law. It declares that its agreement with the alien "has all

the earmarks of a sale" rather than a license (Pet. 22). It then argues that, if a sale, it seemed clear under the law at the time that payments of the annual "license fees" were not subject to the withholding requirements (Pet. 22-24). Leaving aside the question whether or not the agreement was a sale, petitioner's speculation as to the reason for its delinquency is scarcely an argument against denying subrogation.

In any event, petitioner had ample opportunity to introduce evidence. Since it chose not to do so (R. 60, note 1), it cannot now complain that the court below refused to substitute conjecture for fact.[10]

2. There is no conflict of decisions. *McGrath* v. *Dravo Corporation,* 183 F. 2d 709 (C.A. 3), asserted by petitioner to be in conflict, is not. Unlike the instant case, the agent there paid the non-withheld tax and reimbursed itself for the amount paid out of the alien's funds in its own hands, all prior to vesting. Accordingly, the issue in no way concerned the effect of the time limitation in Section 34(a) that the claim be "due and owing at the time of * * * vesting * * *." The opinion contains no reference either to the time limitation or to subrogation and, on its facts, the decision could not

[10] In this connection, it is appropriate to note that as to the vested property, which consisted of license fees coming due under the same agreement, petitioner did withhold and pay the taxes. Furthermore, it does not appear that petitioner ever protested the payment of taxes on any of the license fees, vested or unvested.

possibly involve subrogation. As the court in that case pointed out (183 F. 2d at 713):

> * * * [the alien's] and [the withholding agent's] rights in respect to each other were settled before the vesting order was made.[11]

3. To make out an important federal question, petitioner advances the bare statement that "the case presents an important question of interpretation of the Trading with the Enemy Act * * * in connection with [the] Internal Revenue Code * * *." (Pet. 9). As a matter of fact, while these statutes are relevant for background purposes, the case does not in any sense concern their meaning. All that is involved is the simple issue whether in the particular circumstances of this case petitioner is entitled to the equitable remedy of subrogation against certain vested funds.

However viewed, the case is of little consequence generally. The records of the Office of Alien Property disclose that, of the approximately 46,000 claims against vested property seeking payment of some $450,000,000,[12] there are but two claimants seeking payment of a total of approximately $3,300 on claims asserted, as is petitioner's, because the claimants were compelled after vesting to pay non-withheld taxes.

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[11] It is significant that the court below in the instant case, while considering *Dravo* in another context, did not refer to it at all on the issue of subrogation.

[12] Annual Report, Office of Alien Property, June 30, 1950, p. 67.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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